

**Letter of Findings: 04-20120591  
Sales and Use Tax  
For the Years 2008, 2009, 2010**

**NOTICE:** [IC 6-8.1-3-3.5](#) and [IC 4-22-7-7](#) require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective as of its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register.

**ISSUES**

**I. Sales and Use Tax – "Wrapping Materials and Containers" Exemption.**

**Authority:** [IC 6-2.5-5-9](#); [IC 6-8.1-5-1](#); [45 IAC 2.2-5-16](#); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Indiana Dep't. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012).

Taxpayer protests the imposition of sales tax on certain items it claims are subject to this exemption.

**II. Tax Administration – Negligence Penalty.**

**Authority:** [IC 6-8.1-10-2.1](#); [45 IAC 15-11-2](#).

Taxpayer also protests the imposition of the ten percent negligence penalty.

**STATEMENT OF FACTS**

Taxpayer, an Indiana company, manufactures various lead-based chemicals. Taxpayer does not produce end products, but rather produces chemicals that other manufacturers use in their respective processes to obtain certain desired qualities in the manufacturers' final products. Taxpayer's customers typically purchase Taxpayer's products exempt from sales tax because the customers purchase the items as raw materials for their own respective production processes and because Taxpayer typically ships its products out of state.

Pursuant to a sales and use tax audit for the years 2008, 2009, and 2010, the Indiana Department of Revenue ("Department") assessed Taxpayer additional sales tax, penalty, and interest on steel drums Taxpayer purchased to hold Taxpayer's products for shipping to Taxpayer's customers.

Taxpayer protested the Department's assessment of additional sales tax and penalty on Taxpayer's purchases of the steel drums. A hearing was held on Taxpayer's protest and this Letter of Findings results. Additional facts will be provided as necessary.

**I. Sales and Use Tax – "Wrapping Materials and Containers" Exemption.**

**DISCUSSION**

Taxpayer argues that steel drums it uses to fill with its lead-based chemicals to sell to customers enjoy an exemption under [IC 6-2.5-5-9](#). Taxpayer states that it only receives a small number of the steel drums back from customers. Taxpayer also alleges that federal laws and regulations regarding the nature of Taxpayer's products prohibit customers from returning the steel drums. Therefore, Taxpayer argues, the steel drums should be considered nonreturnable containers.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. [IC 6-8.1-5-1\(c\)](#); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007); Indiana Dep't. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012).

[IC 6-2.5-5-9](#) states:

- (a) As used in this section, "returnable containers" means containers customarily returned by the buyer of the contents for reuse as containers.
- (b) Sales of returnable containers are exempt from the state gross retail tax if the transaction constitutes selling at retail as defined in [IC 6-2.5-4-1](#) and if the returnable containers contain contents.
- (c) Sales of returnable containers are exempt from the state gross retail tax if the containers are transferred empty for the purpose of refilling.
- (d) Sales of wrapping material and empty containers are exempt from the state gross retail tax if the person acquiring the material or containers acquires them for use as nonreturnable packages for selling the contents that he adds.

[45 IAC 2.2-5-16](#) expands upon the above statute:

- (a) The state gross retail tax shall not apply to sales of nonreturnable wrapping materials and empty containers to be used by the purchaser as enclosures or containers for selling contents to be added, and returnable containers containing contents sold in a sale constituting selling at retail and returnable containers sold empty for refilling.
- (b) In general the gross proceeds from the sale of tangible personal property in a transaction of a retail merchant constituting selling at retail are taxable. This regulation [[45 IAC 2.2](#)] provided an exemption for wrapping materials and containers.
- (c) General rule. The receipt from a sale by a retail merchant of the following types of tangible personal

property are exempt from state gross retail tax:

- (1) Nonreturnable containers and wrapping materials including steel strap and shipping pallets to be used by the purchaser as enclosures for selling tangible personal property.
- (2) Deposits for returnable containers received as an incident to a transaction of a retail merchant constituting selling at retail.
- (3) Returnable containers sold empty for refilling.
- (d) Application of general rule.
  - (1) Nonreturnable wrapping material and empty containers. To qualify for this exemption, nonreturnable wrapping materials and empty containers must be used by the purchaser in the following way:
    - (A) The purchaser must add contents to the containers purchased; and
    - (B) The purchaser must sell the contents added.
  - (2) Returnable containers sold at retail with contents. To qualify for this exemption, the returnable containers must be:
    - (A) Sold in a taxable transaction of a retail merchant constituting selling at retail; and
    - (B) Billed as a separate charge by the retail merchant to his customer. If there is a separate charge for such containers, the sale of the container is exempt from tax under this regulation [\[45 IAC 2.2\]](#).
  - (3) Returnable containers sold empty. To qualify for this exemption the returnable container must be resold with the purpose of refilling. The sale of returnable containers to the original or first user thereof is taxable.
- (e) Definitions.
  - (1) Returnable containers. As used in this regulation [\[45 IAC 2.2\]](#), the term returnable container means containers customarily returned by the buyer of the contents for reuse as containers.
  - (2) Nonreturnable containers. As used in this regulation [\[45 IAC 2.2\]](#), the term "nonreturnable containers" means all containers which are not returnable containers.

During the audit, Taxpayer's shop manager deemed the steel drums as returnable. Taxpayer stated that Taxpayer or Taxpayer's accounting representative wanted to look into more information regarding the steel drums. However, Taxpayer did not provide further information to the Department prior to the Department's completion of the audit.

During the administrative hearing, Taxpayer echoed the shop manager's statements, deeming the drums returnable. But Taxpayer argued that the steel drums do not come back to Taxpayer. Further, Taxpayer averred that federal regulations prohibit the return of those drums that contained lead-based materials shipped outside the United States.

The Department requested that Taxpayer provide the alleged federal rules or regulations, as well as any other information that Taxpayer thought supported Taxpayer's arguments. While the Taxpayer subsequently provided a schedule showing that some of the subject steel drums were not returned, Taxpayer did not provide any other information that contradicted the Department's determination that the steel drums were customarily returnable. Taxpayer did not provide evidence sufficient to show that the Department's assessments were inaccurate.

## FINDING

Taxpayer's protest is respectfully denied.

## II. Tax Administration – Negligence Penalty.

### DISCUSSION

The Department issued ten percent negligence penalties for the tax years in question. Taxpayer protests the imposition of the penalties. The Department refers to [IC 6-8.1-10-2.1\(a\)\(3\)](#), which states in relevant part:

If a person:

...

- (3) incurs, upon examination by the department, a deficiency that is due to negligence;

...

the person is subject to a penalty.

The Department refers to [45 IAC 15-11-2\(b\)](#), which states:

"Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The Department may waive a negligence penalty as provided in [45 IAC 15-11-2\(c\)](#), as follows:

The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or

failing to carry out a duty giving rise to the penalty imposed under this section.

Taxpayer has met its burden of proof to show that the deficiencies it incurred are due to reasonable cause and are therefore not subject to a penalty under [IC 6-8.1-10-2.1](#)(a).

**FINDING**

Taxpayer's protest is sustained.

**SUMMARY**

Taxpayer has not provided evidence sufficient to rebut the Department's taxability of the steel drums as returnable containers. Therefore, Taxpayer's protest regarding the steel drums is respectfully denied. However, based upon Taxpayer's assertions during the protest, the Department sustains Taxpayer's protest involving the ten percent negligence penalty, and waives those penalty amounts.

*Posted: 03/26/2014 by Legislative Services Agency*

An [html](#) version of this document.